CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

April 4, 2002

H.R. 3762
Pension Security Act of 2002

As ordered reported by the House Committee on Education and the Workforce on March 20, 2002

SUMMARY

H.R. 3762 would make numerous changes to the Employee Retirement Income Security Act of 1974 (ERISA) that would affect the operations of private pension plans. These include new reporting requirements, limitations on certain investments, modifications in premiums paid to the Pension Benefit Guaranty Corporation (PBGC), and other changes.

CBO estimates that the bill would increase direct spending by $36 million in 2003, by $127 million over the 2003-2007 period, and by $185 million over the 2003-2012 period. Discretionary spending would also increase by $24 million over the 2003-2007 period, assuming appropriation of the necessary amounts. CBO and the Joint Committee on Taxation (JCT) estimate that the bill would have a negligible effect on revenues. Since this bill would affect direct spending and revenues, pay-as-you-go procedures would apply.

State, local, and tribal governments are exempt from the requirements of ERISA that H.R. 3762 would amend, and other provisions of the bill would impose no requirements on those governments. Consequently, the bill would contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

The bill contains several private-sector mandates on sponsors, administrators, and fiduciaries of private pension plans. CBO estimates that the direct cost of those new requirements would exceed the annual threshold specified in UMRA ($115 million in 2002, adjusted annually for inflation), but we do not have sufficient information to provide a precise estimate of the aggregate cost.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 3762 is shown in the following table. The costs of this legislation would fall within budget function 600 (income security).

	By Fiscal Year, in Millions of Dollars					
	2002	2003	2004	2005	2006	2007
DIRECT SPENDING						
Reduced PBGC Flat-Rate Premiums	0	1	1	2	2	2
Changes in PBGC Variable Premiums	0	32	-7	76	*	3
Payment of Interest on						
Overpayments of PBGC Premiums	0	3	3	3	3	3
Benefits Paid to Substantial Owners	0	*	*	*	*	*
Total Additional Outlays	0	36	-3	81	5	8
SPENDING SUBJECT TO APPROPRIATION						
Studies by the Department of Labor						
Estimated Authorizations	0	2	0	0	0	0
Estimated Outlays	0	*	1	*	*	*
Informational and Educational Support for Pension Plan Fiduciaries						
Estimated Authorizations	0	5	5	5	5	6
Estimated Outlays	0	3	5	5	5	5
Total Spending Subject to Appropriation						
Estimated Authorizations	0	7	5	5	5	6
Estimated Outlays	0	3	6	5	5	5
Memorandum:						
Changes in Revenues Resulting from Enactment of Both H.R. 3762 and H.R. 3669 [a]	994	994	-270	-593	-485	-327

NOTES: *= Less than $500,000.

a. These revenue effects reflect changes in pension plan funding and were included in CBO's estimate for H.R. 3669, the Employee Retirement Savings Bill of Rights. Enactment of H.R. 3762 alone would not affect revenues.

BASIS OF ESTIMATE

Revenues

All estimates of the provisions in the bill that affect revenues, except the civil penalties under section 102, were provided by JCT. JCT estimates that none of those provisions would have significant effects on revenue collections. Based on information from the Department of Labor, CBO expects that additional civil penalties resulting from section 102 would be less than $500,000 annually.

If the bill were enacted in combination with H.R. 3669, the Employee Retirement Savings Bill of Rights, which was reported by the Committee on Ways and Means on March 20, 2002, JCT estimates that federal revenues would be increased by $994 million in 2002, but would be reduced by $991 million over the 2002-2012 period. These revenue effects were included in CBO's estimate for H.R. 3669. According to JCT, the revenue effects depend on conforming changes to both the Internal Revenue Code and ERISA, and JCT's estimates for H.R. 3669 assumed that the conforming changes would be enacted.

Direct Spending

Reduced Flat-Rate Premiums Paid to the PBGC. Under current law, defined benefit pension plans operated by a single employer pay two types of annual premiums to the Pension Benefit Guaranty Corporation. All covered plans are subject to a flat-rate premium of $19 per participant. In addition, underfunded plans must also pay a variable-rate premium that depends on the amount by which the plan's liabilities exceed its assets.

The bill would reduce the flat-rate premium from $19 to $5 per participant for plans established by employers with 100 or fewer employees during the first five years of the plan's operation. According to information obtained from the PBGC, approximately 7,500 plans would eventually qualify for this reduction. Those plans cover an average of about 10 participants each. CBO estimates that the change would reduce the PBGC's premium income by about $1 million in 2003, $8 million over the 2003-2007 period, and $18 million from 2003 through 2012. Since PBGC premiums are offsetting collections to a mandatory spending account, reductions in premium receipts are reflected as increases in direct spending.

Changes in Variable Premiums Paid to the PBGC. H.R. 3762 would make several changes affecting the variable-rate premium paid by underfunded plans. CBO estimates, in total, this section will decrease receipts from those premiums by $32 million in 2003, $104 million over the 2003-2007 period, and $137 million during the 2003-2012 period.

First, for all new plans that are underfunded, the bill would phase in the variable-rate premium. In the first year, plans would pay nothing. In the succeeding four years, they would pay 20 percent, 40 percent, 60 percent, and 80 percent, respectively, of the full amount. In the sixth and later years, they would pay the full variable-rate premium determined by their funding status. On the basis of information from the PBGC, CBO estimates that this change would affect the premiums of approximately 250 plans each year. It would reduce the PBGC's total premium receipts by about $19 million over the 2003-2007 period and $46 million over the 2003-2012 period.

Second, the bill would reduce the variable-rate premium paid by all underfunded plans (not just new plans) established by employers with 25 or fewer employees. Under the bill, the variable-rate premium per participant paid by those plans would not exceed $5 multiplied by the number of participants in the plan. CBO estimates that approximately 2,500 plans would have their premium payments to the PBGC reduced by this provision beginning in 2003. As a result, premium receipts would decline by $1 million in 2004, $4 million during the 2004-2007 period, and $10 million over the 2003-2012 period.

Third, the bill would alter the pension funding requirements in ERISA, which would allow plans to become more underfunded in plan year 2001 without subjecting them to tax and other penalties. JCT estimates that this provision would initially cause employers to reduce pension plan contributions, but later increase these contributions until funding returns to baseline levels. Some plans would have to pay higher premiums because their level of underfunding would increase. Other plans, however, would qualify for a special exemption and not be required to pay the variable premium for plan-year 2001. Based on information from the PBGC, CBO estimates that the net effect would be a decrease of $30 million in premium receipts in 2003. CBO estimates H.R. 3762 would increase plan underfunding by about $1.2 billion in 2002, leading to an increase in premium receipts of $11 million in 2004. Over the 2003-2007 period, CBO estimates this provision would cause receipts to decrease by a net of $1 million.

Finally, H.R. 3762 would amend the underlying formula used to determine variable-rate premiums. Changes to ERISA made by the Job Creation and Worker Assistance Act (P.L. 107-147) require that, during plan-years 2002 and 2003, the interest rate used to calculate plans' liabilities be 100 percent of the interest rate on 30-year Treasury securities in the month preceding the month in which the plan year begins. This interest rate will return to 85 percent of the Treasury rate unless and until the Department of the Treasury issues new mortality tables for pension beneficiaries, at which time the liability calculation will be set at 100 percent. Instead, section 212 would set the interest rate at 115 percent of the 30-year bond rate once the new mortality tables are issued, but only through the remainder of plan-years 2002 and 2003, at which time the interest rate would return to 100 percent. As part of its latest baseline projections CBO anticipates that the new mortality tables will be issued immediately before the start of plan-year 2003. Therefore, under CBO's assumptions about when the new mortality tables will be issued, the bill would allow plans to use 115 percent of the 30-year bond rate to determine liabilities in plan-year 2003 before being set at 100 percent of the bond rate thereafter.

Increasing the interest rate effectively lowers the measured amount of underfunding among plans because using higher interest rates reduces projected liabilities, which are calculated on a present-value basis. By reducing the measured level of underfunding, CBO estimates that this provision of section 212 would reduce premium collections by $80 million in 2005.

Authorization for the PBGC to Pay Interest on Premium Overpayment Refunds. The legislation would authorize the PBGC to pay interest to plan sponsors on premium overpayments. Interest paid on overpayments would be calculated at the same rate as interest charged on premium underpayments. On average, the PBGC receives $19 million per year in premium overpayments, charges an interest rate of 8 percent for underpayments, and experiences a two-year lag between the receipt of payments and the issuance of refunds. Based on this information, CBO estimates that direct spending would increase by $3 million annually.

Substantial Owner Benefits in Terminated Plans. H.R. 3762 would simplify the rules by which the PBGC pays benefits to substantial owners (those with an ownership interest of at least 10 percent) of terminated pension plans. Only about one-third of the plans taken over by the PBGC involve substantial owners, and the change in benefits paid to owner-employees under this provision would be less than $500,000 annually.

National Summit on Retirement Income Security. H.R. 3762 would extend the authorization for the National Summit on Retirement Income Security so that meetings would be held in 2006 and 2010. The most recent summit was held in January 2002. Based on donations received for that summit, CBO estimates that the Department of Labor would receive about $500,000 in private donations for each future summit, which would be spent to defray part of the costs of the conferences. Therefore, this provision would increase revenues and direct spending by the same amounts and would have no net impact on the budget surplus.

Discretionary Spending

Studies by the Department of Labor. H.R. 3762 would direct the Department of Labor (DOL) to undertake three studies: one to determine the most appropriate forms of private pension plans, one on the impact of H.R. 3762 on various aspects of pension coverage, and one on the impact of requiring fiduciary consultants for individual account plans. Based on the costs of studies with comparable requirements, CBO estimates these studies would cost about $2 million over the 2003-2007 period.

Informational and Educational Support for Pension Plan Fiduciaries. The bill also would require DOL to provide information and educational resources to persons serving as fiduciaries for employee pension benefit plans. Based on a review of other federal programs that provide consumer-related and technical information to the public, CBO estimates that providing this support would cost about $5 million per year.

National Summit on Retirement Income Security. H.R. 3762 would amend the authorization for the National Summit on Retirement Security to require the President to convene a conference on national savings in 2006 rather than in 2005, and to hold an additional summit in 2010. The appropriation of such sums as may be necessary is authorized for that purpose. The Secretary of Labor is also authorized to accept private donations to defray the costs of the conference, and must spend the donated funds prior to spending the appropriated funds. Based upon the experience of the 1998 and 2002 National Summits, CBO estimates that future summits would cost less than $1 million and that more than one-half of the expenses would be offset by private donations.

PAY-AS-YOU-GO CONSIDERATIONS

The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in outlays and governmental receipts that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects through 2006 are counted.

	By Fiscal Year, in Millions of Dollars										
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Changes in receipts [a]	0	0	0	0	0	0	0	0	0	0	0
Changes in outlays	0	36	-3	81	5	8	11	11	12	12	12

a. Enactment of H.R. 3762 alone would not affect revenues, though there would be a revenue effect if the bill were enacted in conjunction with H.R. 3669.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

State, local, and tribal governments are exempt from the requirements of ERISA that H.R. 3762 would amend, and other provisions of the bill would impose no requirements on those governments. Consequently, the bill would contains no intergovernmental mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

With only limited exceptions, private employers who provide pension plans for their workers must follow rules specified in ERISA. Therefore, CBO considers changes in ERISA that expand those rules to be private-sector mandates under UMRA. H.R. 3762 would make several such changes to ERISA that would affect sponsors, administrators, and fiduciaries of pension plans. CBO estimates that the direct cost to affected entities of the new requirements in H.R. 3762 would exceed the annual threshold specified in UMRA ($115 million in 2002, adjusted annually for inflation), but does not have sufficient information to provide a precise estimate of the aggregate cost.

Benefit Statements. Section 101 of the bill would require administrators of private, individual-account (defined contribution) pension plans to provide quarterly statements to participants and beneficiaries. Those statements would have to contain several items, including the amount of accrued benefits, the amount of nonforfeitable benefits, the value of any assets held in the form of securities of the employing firm, an explanation of any limitations or restrictions on the right of the participant or beneficiary to direct an investment, and an explanation of the importance of a well-balanced and diversified portfolio. Currently, plans must provide more limited statements to participants upon request.

CBO estimates that the direct cost of this new requirement on private plans would be about $100 million annually. An estimated 70 million people will participate in private, individual-account pension plans in 2003. According to industry sources, the majority of plans sponsored by large employers already provide pension statements on a quarterly basis, and it is becoming increasingly common for plans sponsored by smaller employers to do so as well. Thus, CBO estimates that about 30 million participants would newly receive statements four times per year under the bill. The average cost of providing each statement would be small because plans are now required to provide benefit statements on request. Thus, the bill would result in added costs largely for producing and delivering the new statements. Written statements would have to be provided to most participants, but the bill would allow statements to be provided electronically to participants with access to the Internet. (Census Bureau information indicates that in 1997 about 15 percent of workers had access to the Internet at their workplace.)

Section 101 of the bill would also require administrators of private, defined-benefit pension plans to provide vested participants currently employed by the sponsor with a benefit statement at least once every three years, or to provide notice to participants of the availability of benefit statements on an annual basis. CBO estimates that the added cost of this provision would be less than $5 million per year.

Notice of Restriction Periods. Currently, participants in individual-account plans occasionally experience time periods (called "blackout" periods) when they are unable to direct the investment of assets in their accounts. Such periods may occur for administrative reasons–for example, when a plan changes recordkeepers. Section 102 of the bill generally would require plan administrators to provide affected participants with 30 days notice before an anticipated suspension, limitation, or restriction on the ability of participants to direct investments in their accounts. Notice would have to be in writing unless participants had access to the Internet.

CBO estimates that the direct cost to private plans of providing advance notice of upcoming blackout periods would be about $15 million annually. According to a survey conducted by the American Society for Pension Actuaries, blackout periods typically occur for a plan about once every three to four years. Data from the Bureau of Labor Statistics indicate that most participants in individual-account plans are in plans that allow at least some direction of assets and, thus, would be affected by those periods.

Fiduciaries' Liability. Currently, plan fiduciaries generally are not liable for investment decisions made by participants, nor are they liable for the inability of participants to alter their investments during blackout periods. Section 102 of the bill would potentially expand the personal liability of plan fiduciaries during blackouts by removing the current limitation on liability and adding specific new requirements under which they could avoid liability.

Fiduciaries would be required to consider the reasonableness of the length of the blackout period, provide 30 days notice to participants, and act solely in the interest of participants in entering the blackout. This provision would impose a direct cost on the affected entities by increasing their financial exposure during blackouts. CBO does not have sufficient information to estimate that added cost, however, but expects that abiding by the new requirements to avoid liability would add little to their costs.

Investment in Employers' Securities. Section 103 of the bill would require individual-account plans to allow participants to sell securities issued by their employer and acquired through elective deferrals after three years of participation in the plan (or, if the plan so provides, after three years of service with the employer). Participants would also be allowed to sell securities issued by their employer and allocated to their accounts three years after they are allocated to them. (The bill would phase in the requirements in 20 percent annual increments for assets acquired before the effective date of the bill.) Section 103 would also require plans that offer participants securities issued by employers to offer a broad range of investment opportunities.

Both the expansion of participants' allowable investments of future contributions and the phase-in for past contributions would increase the administrative and record-keeping costs of affected pension plans. According to a small survey sponsored by the Employee Benefit Research Institute, 48 percent of surveyed 401(k) plans had company stock as an investment option for participants, and 43 percent of plans with such an option required the employer's contributions to be invested in company stock. CBO estimates that the added administrative costs attributable to these provisions could easily be $20 million annually, with larger amounts in the first year. In addition, the potential sale of the employer's stock by plan participants as a result of these new requirements could temporarily reduce the stock's price, especially for companies whose stock is thinly traded. Finally, requiring plans to offer a range of investment options would probably add little to plan costs because many plans now abide by a safe harbor provision in ERISA that has similar requirements.

Insider Trades. Section 105 of the bill would prohibit certain owners and officers of a company from trading securities issued by that company during a period when participants in the retirement plan are restricted in their ability to direct investments. This restriction would increase the financial exposure of affected owners and officers and, thus, impose a cost on them. CBO does not have sufficient information to estimate the amount of that cost.

PREVIOUS CBO ESTIMATE

On March 20, 2002, CBO provided the Committee on Ways and Means with a cost estimate for H.R. 3669, the Employee Retirement Savings Bill of Rights. That bill contained a number of changes affecting ERISA’s treatment of private pension plans, including some adjustments to the PBGC’s premium formulas, that are similar those contained in H.R. 3762. Although many of the budgetary effects are similar, the estimated change in variable-rate premiums is different. For H.R. 3762, the estimated decrease in receipts from variable-rate premiums is $137 million during the 2003-2012 period, while for H.R. 3669 the estimated decrease is $56 million over the same period. The estimate for H.R. 3669 also reflected changes in pension plan funding that would increase revenues by $994 million in 2002 but reduce them by $991 million over the 2002-2012 period. The JCT revenue estimate for the pension funding effects of H.R. 3669 assumed the conforming changes to ERISA that are included in H.R. 3762. H.R. 3669 also included changes to the Internal Revenue Code, the Federal Insurance Contribution Act, and the Federal Unemployment Tax Act that would reduce revenues by $23.4 billion over the 2003-2012 period.

ESTIMATE PREPARED BY:

Federal Revenues: Erin Whitaker
Outlays of the Pension Benefit Guaranty Corporation: Geoff Gerhardt
Other Spending by the Department of Labor: Christina Hawley Sadoti
Impact on State, Local, and Tribal Governments: Leo Lex
Impact on the Private Sector: Bruce Vavrichek

ESTIMATE APPROVED BY:

Robert A. Sunshine
Assistant Director for Budget Analysis

G. Thomas Woodward
Assistant Director for Tax Analysis